



Invest to prevent disaster

A Re-Insurer's Foundation Perspective on Microfinance

Written by

Dirk Reinhard

Vice Chair of the
Foundation, Munich Re

Foundation From

Knowledge to Action

dreinhard@munichre-foundation.org

www.munichre-foundation.org

1. From your experience, can microfinance be a tool to reduce the impact of disasters?

Microfinance is regarded as an important tool to reduce poverty and experience shows that poor people are usually extremely vulnerable to disasters. Since there is a link between poverty and vulnerability, there is consequently a link between microfinance and vulnerability. However, microfinance alone is not sufficient as a disaster reduction tool; it needs to be supplemented by microinsurance. The products needed are those tailored to the different populations affected by disasters and targeted at various levels—from the individual (small scale) to government (large scale). Furthermore, microinsurance and other tailor-made insurance products have to be strengthened by reinsurance.

2. In this context, what are the main limits or constraints of this tool?

There are a number of challenges for using microinsurance as a disaster reduction tool. Several of these apply equally to microfinance.

Identifying clients can be difficult as often they lack education or are illiterate, and infrastructure may be inadequate. Therefore, innovative approaches to raising awareness and new channels of product distribution are necessary. For example, street theatres might be useful to explain the mechanisms of insurance. A community representative or organization should organize the premium collection as it would have better access to the local people. Another constraint is that the premiums are often paid irregularly (because of poor harvests, for example). Furthermore, poor people often do not understand the purpose and benefit of insurance. They often question why they do not receive their money back if they make no claims. Another very important concern is the necessity for adequate consumer-protection regulations (especially for illiterate populations). It should be kept in mind that in some cases humanitarian concerns and commercial concerns are at cross-purposes.

Understanding local conditions is vital as the administrative costs are very high and can only be reduced by close cooperation among all stakeholders. Another obstacle to overcome is that often microfinance initiatives do not have enough insurance knowledge. Partnerships between local organizations and insurance companies are therefore ideal. Also, political and legal frameworks may be unstable or even inexistent. Other concerns include that reinsurance is scarcely available, products are often difficult to understand and lack of data (e.g. no claims history) requires innovative quotation tools.

To overcome these obstacles, it is essential to include the insurance industry, which holds important experience, in the process of developing microinsurance solutions. Frequently the financing (development) of microinsurance is a challenge.

3. What are the best conditions for the optimal functioning of microinsurance?

Products should be easy to understand. In addition, premiums should be low (depending on the size of the solidarity community) so that only a small proportion of income is attributed to the insurance premium. Small but frequent payments (e.g. weekly) are necessary. The insured population should be aggregated in order to attract professional insurers and reinsurers, as group insurance is most cost efficient. Above all, it should be clear who benefits from the insurance (the insured or the financial institution).